

partnership item is inconsistent with the treatment of the item by P.

Example 2. Partnership P incurred certain start-up costs before P was actively engaged in its business. P capitalized these costs. C, a partner in P, deducted C's proportionate share of these start-up costs. C's treatment of the partnership expenditure is inconsistent with the treatment of that item by P.

Example 3. D is a partner in partnership P. P reports a loss of \$100,000 on its return, \$5,000 of which it reports on the Schedule K-1 attached to its return as D's distributive share. However, P reports \$15,000 as D's distributive share of P's loss on the Schedule K-1 furnished to D. D reports the \$15,000 loss on D's income tax return. D has not satisfied the consistent reporting requirement. See, however, § 301.6222(b)-3 for an election to be treated as having reported the inconsistency.

(d) *Effective date.* This section is applicable to partnership taxable years beginning on or after October 4, 2001.

For years beginning prior to October 4, 2001, see § 301.6222(a)-1T contained in 26 CFR part 1, revised April 1, 2001.

[T.D. 8965, 66 FR 50545, Oct. 4, 2001]

§ 301.6222(a)-2 Application of consistent reporting and notification rules to indirect partners.

(a) *In general.* The consistent reporting requirement of § 301.6222(a)-1 is generally applied with respect to the source partnership. For purposes of this section, the term *source partnership* means the partnership (within the meaning of section 6231(a)(1)) from which the partnership item originates.

(b) *Indirect partner files consistently with source partnership.* An indirect partner who treats an item from a source partnership in a manner consistent with the treatment of that item on the source partnership's return satisfies the consistency requirement of section 6222(a) regardless of whether the indirect partner treats that item in a manner consistent with the treatment of that item by the pass-thru partner through which the indirect partner holds the interest in the source partnership. Under these circumstances, therefore, the Internal Revenue Service shall not send to the indirect partner the notice described in section 6231(b)(1)(A).

(c) *Indirect partner files inconsistently with source partnership—(1) Indirect partner notifies the Internal Revenue*

Service of inconsistency. An indirect partner who—

(i) Treats an item from a source partnership in a manner inconsistent with the treatment of that item on the source partnership's return; and

(ii) Files a statement identifying the inconsistency with the source partnership in accordance with § 301.6222(c)-1, shall not be subject to a computational adjustment to conform the treatment of that item to the treatment of that item on the return of the source partnership.

(2) *Indirect partner does not notify the Internal Revenue Service of inconsistency.* Except as provided in paragraph (b)(3) of this section, an indirect partner who—

(i) Treats an item from a source partnership in a manner inconsistent with the treatment of that item on the source partnership's return; and

(ii) Fails to file a statement identifying the inconsistency with the source partnership in accordance with § 301.6222(b)-1, is subject to a computational adjustment to conform the treatment of that item to the treatment of that item on the return of the source partnership.

(3) *Indirect partner files consistently with a pass-thru partner that notifies the Internal Revenue Service of the inconsistency.* If an indirect partner treats an item from a source partnership in a manner consistent with the treatment of that item by a pass-thru partner through which the indirect partner holds the interest in the source partnership and that pass-thru partner—

(i) Treats that item in a manner inconsistent with the treatment of that item on the source partnership's return; and

(ii) Files a statement identifying the inconsistency with the source partnership in accordance with § 301.6222(b)-1, the indirect partner is not subject to a computational adjustment to conform to the treatment of that item on the return of the source partnership.

(d) *Examples.* The following examples illustrate the principles of this section:

Example 1. One of the partners in Partnership A is Partnership B, which has four equal partners C, D, E, and F. Both A and B are partnerships within the meaning of section 6231(a)(1). On its return, A reports \$100,000 as

B's distributive share of A's ordinary income. B, however, reports only \$80,000 as its distributive share of the income and does not notify the Internal Revenue Service of this inconsistent treatment with respect to A. C reports \$20,000 as its distributive share of the item. Although C reports the item consistently with B, C is subject to a computational adjustment to conform the treatment of that item on C's return to the treatment of that item on A's return.

Example 2. Assume the same facts as in Example 1, except that B notified the Internal Revenue Service of its inconsistent treatment with respect to source partnership A. C is not subject to a computational adjustment.

Example 3. Assume the same facts as in Example 1. D reports only \$15,000 as D's distributive share of the income and does not report the inconsistency. F reports only \$9,000 as its distributive share of the item but reports this inconsistency with respect to source partnership A. D is subject to a computational adjustment to conform the treatment of that item on D's return to the treatment of that item on A's return. F is not subject to a computational adjustment.

Example 4. Assume the same facts as in Example 3, except that F reported the inconsistency with respect to B and did not report the inconsistency with respect to source partnership A. F is subject to a computational adjustment to conform the treatment of that item on F's return to the treatment of that item on A's return.

Example 5. Assume the same facts as in Example 1. E reports \$25,000 as its distributive share of the item. Regardless of whether E reports the inconsistency between its treatment of the item and that by B, E is neither subject to a computational adjustment to conform E's treatment of that item to that of B nor subject to the notice described in section 6231(b)(1)(A) with respect to any such notification of inconsistent treatment.

(e) *Effective date.* This section is applicable to partnership taxable years beginning on or after October 4, 2001. For years beginning prior to October 4, 2001, see § 301.6222(a)-2T contained in 26 CFR part 1, revised April 1, 2001.

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§ 301.6222(b)-1 Notification to the Internal Revenue Service when partnership items are treated inconsistently.

(a) *In general.* The statement identifying an inconsistency described in section 6222(b)(1)(B) shall be filed by filing the form prescribed for that purpose in accordance with the instructions accompanying that form.

(b) *Effective date.* This section is applicable to partnership taxable years beginning on or after October 4, 2001. For years beginning prior to October 4, 2001, see § 301.6222(b)-1T contained in 26 CFR part 1, revised April 1, 2001.

[T.D. 8965, 66 FR 50546, Oct. 4, 2001]

§ 301.6222(b)-2 Effect of notification of inconsistent treatment.

(a) *In general.* Generally, if a partner treats a partnership item on the partner's return in a manner inconsistent with the treatment of that item on the partnership return, the Internal Revenue Service may make a computational adjustment to conform the treatment of the item by the partner with the treatment of that item on the partnership return. Any additional tax resulting from that computational adjustment may be assessed without either the commencement of a partnership proceeding or notification to the partner that all partnership items arising from that partnership will be treated as nonpartnership items. However, if a partner notifies the Internal Revenue Service of the inconsistent treatment of a partnership item in the manner prescribed in § 301.6222(b)-1, the Internal Revenue Service generally may not make an adjustment with respect to that partnership item unless the Internal Revenue Service—

(1) Conducts a partnership-level proceeding; or

(2) Notifies the partner under section 6231(b)(1)(A) that all partnership items arising from that partnership will be treated as nonpartnership items. See, however, §§ 301.6231(c)-1 and 301.6231(c)-2 for special rules relating to certain applications and claims for refund based on losses, deductions, or credits from abusive tax shelter partnerships.

(b) *Partner protected only to extent of notification.* (1) A partner who reports the inconsistent treatment of partnership items on the partner's return is protected from computational adjustments under section 6222(c) only with respect to those partnership items the inconsistent treatment of which is reported. Thus, if a partner notifying the Internal Revenue Service with respect to one item fails to report the inconsistent treatment of another item, the partner is subject to a computational